



Global Insight

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Narrowing leadership

In one important sense, stocks are behaving as one would expect. Leading the way are shares of companies whose businesses are thriving and for whom the post-pandemic world looks bright—big tech comes immediately to mind. At the other end of the spectrum are shares of companies whose business conditions are challenging and might remain so after COVID-19 departs the scene—oil and gas for instance or bricks and mortar retailing.

This distinction is even more sharply drawn than usual because, for the most affected parts of the economy, the longer the pandemic keeps economic activity well below normal the greater the chance some established businesses won't survive. So investors, understandably, have chosen to move more decisively than usual toward companies for whom the risk of failure seems very low and the promise of above-average sales and earnings growth appears assured.

So far, so good, as long as the market's assessment of future business prospects is correct. And this relative shift can go on for a long time; back at the peak of the decade-long oil/commodity boom in 1980, the five largest U.S. oil stocks accounted for more than 40% of total S&P 500 value. The Technology sector reached

Equity views

Region	Current
Global	–
United States	–
Canada	–
Continental Europe	=
United Kingdom	–
Asia (ex-Japan)	+
Japan	=

+ Overweight = Market Weight – Underweight
Source - RBC Wealth Management

similar proportions at the peak of the dot-com boom in 2000.

But at some point the market may come to give today's highly favored, sought-after mega-cap leaders more than they are due. It becomes a more problematic phase when market leaders are going up faster than the broad market simply because they have already been going up faster than the market.

To some extent that phase may be upon us. From the bottom of the market in March until June, the S&P 500 unweighted index—which gives an equal weight to each stock—was doing as well or better than the S&P 500 capitalization-weighted index. Since then, the large caps have taken charge and even within that category the leadership has progressively

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For important and required non-U.S. analyst disclosures, see page 4.

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narrowed in recent weeks to just a handful of mega-cap issues big enough to drive the index higher on their own.

This can go on for some time. But to the extent this phenomenon forces fund managers to buy into stocks they might otherwise have not chosen to own just to keep pace with the benchmark or makes others reluctant to sell the same issues, it can build distortions into the market

which, if they eventually unwind, can be painful for market performance.

This by itself is not a reason to become overtly defensive but it is a risk factor that was not present just a few months ago or for a long time before that.

Our stance has not changed. A global portfolio should carry an exposure to equities modestly below benchmark.

Research resources

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